

The Disruptive Discoveries Journal

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China, Minor Metals, and Supply Chains Over the Next Five Years

With attention focused on Greece and the brinksmanship on display, it was refreshing last week to focus on another topic and participate in a roundtable discussion on the development path for China and its minor metals business over the next five years. The seminar, held in New York and hosted by [TREM](#) and [MMTA](#) (two important think tanks focused on the strategic metals space), hosted numerous individuals across metals value chains, from traders, to strategists, to trade lawyers to investment professionals. I participated as a panelist with a group emceed by Clint Cox, founder of [The Anchor House](#), an exceptional think tank on rare earth element matters.

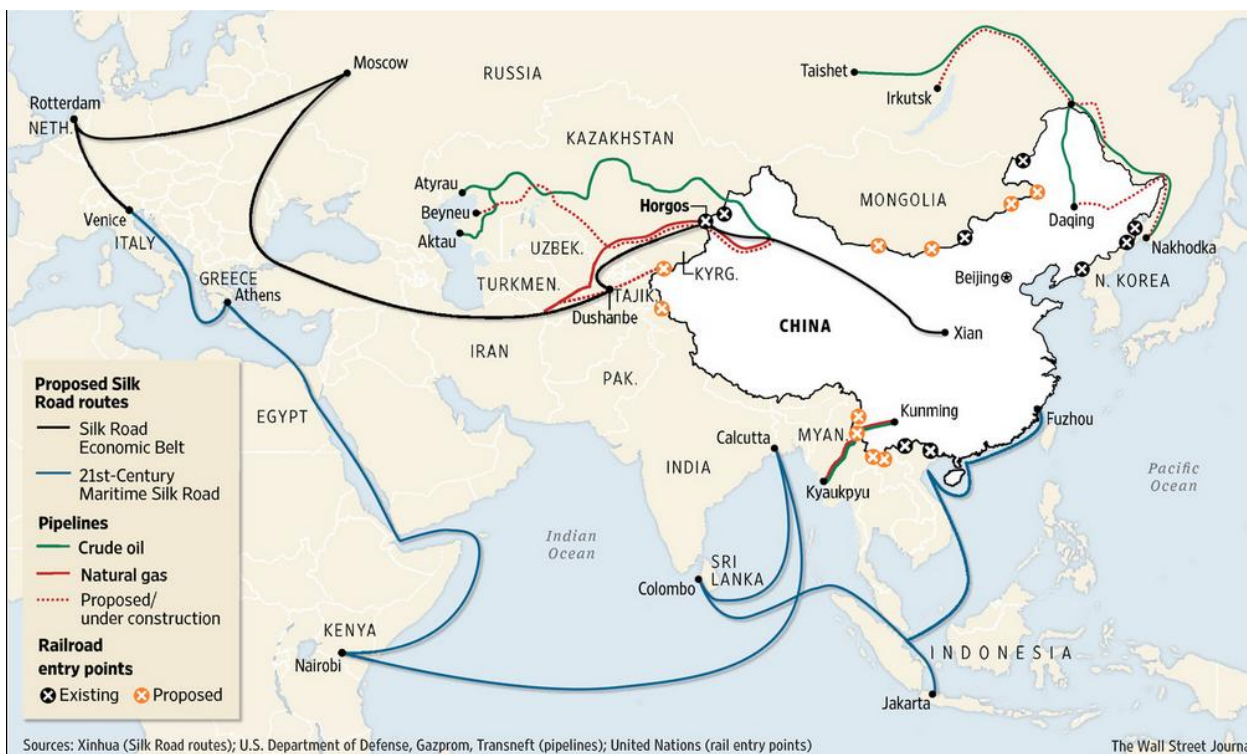
What We Found Out

The seminar was more “macro” in substance and was a refreshing change from the typical conference where you’re pitched by a litany of REE juniors all trying to prove their worth. The conference centered on the methods China’s leaders are employing to build sustainable domestic supply chains and evolve China’s manufacturing base. Chinese President Xi Jinping has spent much of his tenure rooting out corruption and consolidating power while at the same time transitioning an economy drowning in debt from investment-led growth to consumption-led growth. Whether or not this is possible was a subject of much debate at the TREM conference with no clear answer. The one point many agreed upon was that China’s model of growth must evolve.

This has perhaps been addressed with the introduction of [Made in China 2025](#), a blueprint for the next generation of manufacturing in the country. The blueprint’s fundamental idea is to enhance and upgrade Chinese manufacturing processes from a focus on quantity to a focus on quality regardless of the industry size. In fact, it appears that the blueprint is geared more towards small and medium size enterprises, companies instrumental in job growth – a fundamental underpinning of a stable Chinese society. The blueprint is focused on ten sectors: new advanced information technology, automated machine tools and robotics, aerospace and aeronautical equipment, maritime equipment and high-tech shipping, modern rail transport, new energy vehicles, power equipment, agricultural equipment, new materials, and biopharmaceuticals and advanced medical products. One conference participant remarked that this is a “qualitative industrial revolution” in the making.

The goals of the Made in China blueprint are designed to enhance manufacturing which in turn shines a very important light on reliable raw material access. If this plan highlights anything, it is that it's more than just those of us in the West that are concerned about security of supply of metals and materials. China plans on sourcing 40% of manufacturing components domestically by 2020 and 70% by 2025. While it is true that trade flows are global in nature, publicly stated goals such as these make it clear that domestic Chinese industry has its own ideas on how to evolve and enhance self sufficiency. Technological independence is presumably also an unstated goal.

At last week's seminar, this idea of self sufficiency was discussed in other areas of the economy as well. The founding of the Asian Infrastructure Investment Bank (AIIB) by China, a \$100 billion fund which now boasts close to 60 members (not including the US!) is one example as is the construction of a new Silk Road designed to more closely integrate Chinese economic interests with a majority of the world's population.



These goals are not only designed to further China's status as a global economic superpower, but also add hundreds of billions of dollars in purchasing power might to its economy.

The goal of the Chinese Renminbi (RMB) becoming a global reserve currency parallels China's enhancement of its economic might on the global stage. While much needs to happen to make this a reality, conference attendees agreed that the foundations are being put in place. One step in bringing this to fruition is having the RMB included in the IMF's [Special Drawing Rights \(SDRs\)](#), a basket of currencies which are currently comprised of USD, EUR, JPY, and GBP. An opening of China's capital account and making the RMB "freely usable" are keys to accomplishing this. With President Xi's plan to increase foreign direct investment to \$1.25 trillion in the next ten years up from \$870 billion in 2014, the aim of the Chinese leadership is clear. It's also notable that China's appetite for gold remains intact.

Gold Hunger

China and India are the dominant buyers.

Top consumers in the first quarter of 2015

Country	Gold demand, in metric tons	Share of global demand
China	273	32.0%
India	192	22.5
Germany	34	4.0
U.S.	32	3.8
Thailand	23	2.7

Source: World Gold Council

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Challenges Remain

The conference last week was incredibly valuable because of the willingness of participants to acknowledge the many challenges China faces in its bid to reshape global trade flows and its economy. Pollution which cannot be ignored anymore, a debt to GDP ratio of 282% according to McKinsey, slowing economic growth (measured a host of different ways), rampant stock market speculation, and cyber espionage were all issues discussed. Chinese leadership must reckon with these challenges. While some of these issues can be dealt with through currency manipulation, a key takeaway was that devaluation was not the answer – deleveraging was. This is likely China's greatest challenge. There are no easy answers as deleveraging is painful and any moves here won't just affect China, but will also affect an increasingly integrated global economy.

To borrow a phrase from my friend Dan McGroarty, minor metals are taking on major implications. This was obvious at the conference. The country which builds supply chains around these materials can be a leader in shaping significant geopolitical and economic issues in the future. Based on China's recent moves, it appears this fact isn't lost on the country's leadership and over the next ten years, the Middle Kingdom is intent on achieving this important goal.

One of my fellow panelists said that China appears intent on "speaking like Deng, and hitting like Mao". Is the rest of the world up for the challenge?

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